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IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

AMERICAN DEPOSIT CORP. and BLACKFEET NATIONAL BANK,

Petitioners,

v.

JAMES W. SCHACHT, individually and as Acting Director of Insurance of the State of Illinois,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

In 1945, in response to the decision in *United States* v. *South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), an antitrust case that held, contrary to the prior understanding, that insurance was interstate commerce, Congress enacted the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-12. That statute provides that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, ... unless such Act specifically relates to the business of insurance." 15 U.S.C. § 1012(b).

1. Did the court of appeals in this case err in holding, contrary to this Court's opinions in *Barnett Bank* v. *Nelson*, 116 S. Ct. 1103 (1996), and *NationsBank* v. *Variable Annuity Life Ins. Co.*, 115 S. Ct. 810 (1995), that the McCarran-Ferguson Act permits a state, under the guise of "regulating the business of insurance," to prevent a national bank from exercising a power that the federal regulatory authorities have recognized is expressly conferred on the bank by the National Bank Act of 1864?

2. Did the court of appeals err in refusing to recognize, in square conflict with the Eighth Circuit in *First Nat'l Bank of Eastern Arkansas* v. *Taylor*, 907 F.2d 775 (8th Cir.), *cert. denied*, 498 U.S. 972 (1990), that in enacting the McCarran-Ferguson Act "Congress did not intend the 'business of insurance' to encompass lawful activities of national banks"?

3. Did the court of appeals err in holding, contrary to this Court's opinion in *NationsBank* v. *Variable Annuity Life Ins. Co.*, *supra*, that the issuance of annuity contracts by national banks constitutes "the business of insurance" within the meaning of the McCarran-Ferguson Act?

PARTIES TO THE PROCEEDING

The names of all parties appear in the caption of the case. Neither petitioner has any nonwholly owned subsidiary.

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PETITION FOR A WRIT OF CERTIORARI

American Deposit Corp. and Blackfeet National Bank respectfully petition the Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit in this proceeding.

I. CITATIONS BELOW, JURISDICTION, AND STATUTES INVOLVED

The case in the lower courts is reported at 84 F.3d 834 (7th Cir. 1996), and 887 F. Supp. 1066 (N.D. Ill. 1995) (magistrate judge's opinion). The opinion of the court of appeals was issued on May 13, 1996. This Court has jurisdiction under 28 U.S.C. § 1254.

The case chiefly involves certain sections of the National Bank Act, especially 12 U.S.C. § 24; the

McCarran-Ferguson Act, 15 U.S.C. §§ 1011-12; and various sections of the Illinois Insurance Code; all of which are printed in the Appendix ("App.").

II. STATEMENT OF THE CASE

A. Background

Petitioner Blackfeet National Bank makes available to depositors a type of deposit called the "Retirement CD." [1] It works thus: The depositor normally will make no withdrawal until an agreed-upon maturity date, during which time interest is accumulated and added to the account. Thereafter, the depositor will receive equal monthly (or other periodic) withdrawals for life, the size of which is determined in relation to the account balance at maturity and the depositor's life expectancy. If the depositor dies before the aggregate of all withdrawals received add up to the full amount of the maturity balance, the difference is paid to the depositor's estate or designated beneficiary.[2] As between bank and depositor, the Retirement CD fits the conventional definition of a deferred refund life annuity contract.[3]

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[1] The Retirement CD is proprietary to petitioner American Deposit Corp. ("ADC"), which licenses it to Blackfeet.

[2] This is a highly simplified description. More details are in the majority opinion below and in the determinations of the OCC and the FDIC. App. 2a, 98a-99a, 116a-117a.

[3] An *annuity* is "[a] right to receive fixed, periodic payments, either for life or for a term of years," or, it should be added, in perpetuity. BLACK'S LAW DICTIONARY 90 (6th ed. 1990), *sub nom.* "Annuity." The most familiar type is the *life* annuity, under which payments are made for the annuitant's life, but there are also *term* annuities, where the payments are

The Office of the Comptroller of the Currency ("OCC"), the governing regulatory authority for national banks, has determined that acceptance of Retirement CD deposits falls squarely within the express core powers conferred on national banks by the National Bank Act of 1864, in particular, the powers to enter into contracts and to receive deposits. App. 97a-114a; 12 U.S.C. § 24 (Third) and (Seventh). The OCC concluded in sum that "*the product represents the very essence of banking which is embodied in a bank's express authority* to accept deposits and enter into contracts, and authority to incur liabilities and fund its operations," App. 103a; it "*is clearly a financial product whose primary attributes are grounded in the Bank's expressly authorized powers.*" App. 104a. (Emphasis added.)

Such a conclusion by the OCC, if reasonable, is determinative under the "*Chevron* doctrine," *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837 (1984), as this Court strongly emphasized in *NationsBank* v. *Variable Annuity Life Ins. Co.*, 115 S. Ct. 810 (1995) ("*NationsBank*"). Accordingly, under ordinary circumstances no state could interfere with a national bank's acceptance of Retirement CD deposits, because from the beginning it has been recognized that a state cannot interfere with a national

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made over a defined term of years, and *perpetual* annuities, which go on forever. A *refund* annuity is one in which the annuitant or his estate or beneficiary is guaranteed to receive back the amount of the principal invested. A *deferred* annuity (versus an *immediate* annuity) is one in which a period of time elapses before payments begin. An *annuity contract* is an agreement to issue an annuity. (Often "annuity" is used as shorthand for "annuity contract.")

bank's exercise of its federally conferred powers, *Barnett Bank* v. *Nelson*, 116 S. Ct. 1103 (1996) ("*Barnett Bank*"), a rule that extends back to *McCulloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819). In addition, the Federal Deposit Insurance Corporation has ruled that the Retirement CD is an insured deposit for federally insured depository institutions. App. 115a-126a.

Respondent Schacht, the Acting Director of Insurance for Illinois, nevertheless asserts authority to prevent national banks from soliciting or receiving Retirement CD deposits from Illinois residents. Retirement CDs are annuity contracts; Illinois law treats annuities as a type of "insurance"; and under Illinois law, insurance business may not be transacted without an Illinois certificate of authority, which Blackfeet does not and cannot have. App. 3a.

That the Retirement CD is confirmed by the OCC to be within the express powers that national banks have held by congressional grant since 1864 is of no moment, in Schacht's view, because of the McCarran-Ferguson Act. That statute was enacted in 1945 in response to this Court's decision in *United States* v. *South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), which overruled its holding in *Paul* v. *Virginia*, 75 U.S. (8 Wall.) 168 (1869), that a contract of insurance is not a transaction in commerce, and upheld a Sherman Act prosecution against insurance companies for price-fixing. Subsection (a) of McCarran-Ferguson's second section, codified as 15 U.S.C. § 1012(a), relieves state regulation of the "business of insurance" from the constraints of the dormant Commerce Clause. More important here, subsection (b), 15 U.S.C. § 1012(b), prevents affirmative preemption of state regulation by federal statutes in certain specified circumstances:

> "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance ... unless such Act specifically relates to the business of insurance: *Provided*, that after June 30, 1948, [the Sherman, Clayton, and FTC Acts] shall be applicable to the business of insurance to the extent that such business is not regulated by State law."

Respondent has accordingly ordered Blackfeet to cease and desist from offering to accept Retirement CD deposits from Illinois residents.

Petitioners filed suit in the district court for the Northern District of Illinois for a declaration and injunction against Schacht under 42 U.S.C. § 1983, the National Bank Act, and other statutory and constitutional provisions. The district court had jurisdiction under 28 U.S.C. §§ 1331 and 1337. The magistrate judge to whom the case was assigned held for Schacht. The court of appeals affirmed in a 2-1 decision (Cummings and Wood, JJ.), over a vigorous 42-page dissent by Judge Flaum. This petition follows.

B. The Majority and Dissenting Opinions

1. *The Majority Opinion*

Despite *Chevron*, the majority paid scant attention to the OCC's determination that the activity involved falls within the core powers conferred on national banks by the National Bank Act. Instead, the majority focused on McCarran-Ferguson questions. It held that annuities are insurance, so that the business of issuing them constitutes "the business of insurance." This conclusion, in turn, rested

on the majority's interpretation of three decisions of this Court. First, the majority narrowly restricted this Court's holding in *NationsBank*, which dealt with the question whether annuities are "insurance." Second, it sought to apply the three-factor "*Pireno* test" derived from this Court's decision in *Union Labor Life Ins. Co.* v. *Pireno*, 458 U.S. 119 (1982) ("*Pireno*"), a test formulated for determining what ancillary activities of *insurance companies* constitute "the business of insurance." Third, the majority understood this Court's decision in *Barnett Bank* to hold that "the [National] Bank Act, just like any other federal law, is within the reach of the McCarran-Ferguson Act."

First: *NationsBank*. The majority's consideration of *NationsBank* was strikingly perfunctory. There, Justice Ginsburg for a unanimous Court had applied the *Chevron* doctrine and upheld the OCC's determination that annuities are not "insurance" under 12 U.S.C. § 92, which (at least arguably) forbids national banks from selling insurance in towns of more than 5000 population. The majority brushed aside her opinion in a single paragraph. "First," it said, "the [*NationsBank*] holding was limited to the brokering, not underwriting, of annuities. . . . Second, the holding was limited to whether federal law precluded a national bank from brokering annuities, not whether a bank doing so—much less a bank underwriting annuities—would be subject to state regulation." App. 8a (citations and footnote omitted).

Second: The *Pireno* Criteria. The majority then sought to apply to the Retirement CD the "*Pireno* test" for determining whether a practice is part of the "business of insurance":

> "*[F]irst*, whether a practice has the effect of transferring or spreading a policyholder's risk; *second*, whether the practice is an integral part of the policy relationship between the insurer and the insured; and *third*, whether the practice is limited to entities within the insurance industry."

Pireno, *supra*, 458 U.S. at 129. It bears repeating that this test was formulated for determining what ancillary activities of insurance companies constitute "the business of insurance" for McCarran-Ferguson purposes, not for determining whether the exercise of express powers by a federally-chartered non-insurance entity is "the business of insurance." The majority, however, regarded the test as fully applicable to the present quite different situation and concluded that annuities are part of the business of insurance.

As to the first criterion, the majority said that annuities do transfer and spread a risk: the "mortality risk" of outliving one's assets. The Retirement CD, it said (echoing the very language of the Fifth Circuit panel that this Court reversed in *NationsBank*, see p. 20 *infra*), "involves both fundamental characteristics of insurance: a mortality risk and a guaranteed return," citing *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. 65 (1959) ("*VALIC*"), in which this Court held that an arrangement must relieve the investor of all risk in order to be exempt from regulation as a *security* under the securities laws.

As to the second *Pireno* criterion, the majority said that the Retirement CD "is not only an 'integral part' of the policy relationship between the insurer and the insured, it is the very document that evidences that relationship." App. 14a.

The majority gave two reasons for holding that the Retirement CD passes the third *Pireno* criterion. One was because it "is an annuity, virtually all of which are issued by insurance companies," referring to a statement in a 1994 magazine article. The other was the fact that 42 states "consider annuities to be an insurance company activity and regulate them as such." App. 14a.

The majority concluded, therefore, that "[b]ecause the sale of the Retirement CD satisfies each of the Supreme Court's *Pireno* criteria, ... the Retirement CD is properly considered the 'business of insurance' for purposes of the McCarran-Ferguson Act." App. 16a.[4]

Third: *Barnett Bank*. In holding that the National Bank Act does not "specifically relate to the business of insurance," App. 16a-17a, the majority turned to Justice Breyer's opinion for a unanimous Court last Term in *Barnett Bank*, *supra*, which held that McCarran-Ferguson "reverse preemption" does

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[4] The majority sought to bolster its conclusion with a snippet from a memorandum of the National Association of Insurance Commissioners which was attached to supplemental remarks in the Congressional Record: a single mention of "annuity *insurance*" buried in a list of 22 different things that were regulated by the New York insurance commissioner. App. 15a. Nothing in this obscure item suggests that Congress was departing from the universal understanding in 1945 that annuities are not insurance. The legislative history of McCarran-Ferguson is voluminous, extending over two years and two Congresses, and deals almost entirely with antitrust considerations. As Judge Flaum observed, "*the entire legislative history contains not a single reference to 'annuities'* by any member of Congress or any witness during the debates and testimony which resulted in the Act." App. 28a n.24 (emphasis added). The majority nowhere mentions this fact or reviews the legislative history itself.

not permit a state to forbid a national bank from exercising the power granted by *12 U.S.C. § 92* to sell insurance in small towns. The majority said that the relevant provisions of the National Bank Act committed "exactly" such an "inadvertent federal intrusion" upon state regulation as was "warned against" in *Barnett Bank*. App. 17a. It further read *Barnett Bank* as inconsistent with any idea that the National Bank Act's conferral of powers on national banks is any less subject to McCarran-Ferguson preemption than any other statute; otherwise, it reasoned, the Court would not have considered whether 12 U.S.C. § 92 specifically relates to the business of insurance. App. 18a. The majority concluded that "[g]iven *Barnett Bank*, we believe that the Bank Act, just like any other federal law, is within the reach of the McCarran-Ferguson Act." *Ibid.*

2. *The Dissenting Opinion*

Judge Flaum's 42-page dissent is comprehensive and scholarly. With extensive quotations from the authorities, it rebuts every point made by the majority, and addresses many additional points which the majority simply ignored.

After pointing out that the definition of "insurance" for McCarran-Ferguson purposes is a federal, not a state, law question, App. 22a, he considered in detail Justice Ginsburg's opinion in *NationsBank*. Rejecting the majority's brushoff of that case, he pointed out that the fact that the opinion—

> "appropriately limited its holding to the actual case before it ... does not suggest that we should ignore the approach taken by the Court and the reasoning and authorities upon which it relied. Ultimately, in my judgment, the Court's

> analysis in *NationsBank* strongly points to the determination that the selling of annuities by national banks is not reasonably regarded as the business of insurance."

App. 25a.

He began by quoting Justice Ginsburg's discussion in *NationsBank* that an annuity is "like putting money in a bank account," and that by offering annuities banks are "*essentially offering financial investment instruments* ... ," App. 25a, quoting 115 S.Ct. at 814 (emphasis Judge Flaum's); "[h]ence the Court accepted the view that annuities are properly described as 'investment instruments' and are analogous to bank accounts." App. 26a. "The Court," he pointed out, "considered and rejected the proposition that a historical association of insurance companies with a particular product mandated the conclusion that the product is 'insurance,'" just as the fact that life insurance companies offer loans does not make lending money "insurance." *Ibid.* He pointed out that the *NationsBank* opinion "also recognized that most states have regulated annuities as insurance, but noted that this regulation had more to do with the fact that insurance companies are likely to sell annuities than with a conclusion that annuities are insurance." *Ibid.*

Judge Flaum noted *NationsBank*'s especially significant recognition that "the key feature of insurance is that it *indemnifies loss*," while annuities "serve an important *investment purpose* and are functionally similar to other investments that banks typically sell" (emphasis Judge Flaum's). App. 27a, quoting from 115 S. Ct. at 816.

Judge Flaum discussed at some length *NationsBank*'s rejection of the notion espoused by the majority that "annuities resemble insurance because

some annuities contain a mortality risk element." App. 27a, summarizing and quoting from 115 S. Ct. at 816. *This aspect of* NationsBank *is of overriding importance here, because the majority had relied on the very reasoning adopted by the Fifth Circuit panel that was categorically rejected by this Court in* NationsBank. *Variable Annuity Life Ins. Co.* v. *Clarke*, 998 F.2d 1295 (5th Cir.), *reh'g en banc denied*, 13 F.3d 833 (1994). See p. 21 *infra*.

Judge Flaum then turned to the legal literature, noting that this Court has shown a readiness to look to it for guidance as to the meaning of "insurance" and "the business of insurance." "After reviewing this literature in regard to the question now before us," he said, "I find that it is nearly unanimous in directing us to the conclusion that the selling of a specialized annuity by a national bank is not 'the business of insurance.' " App. 28a. He then worked in detail through one leading treatise and law encyclopedia after another, with lengthy discussion and extensive quotation from each. App. 28a-38a, summarized in note 11 *infra*. After this examination he said:

> "By now, the refrain is more than familiar to the reader. The focus on indemnifying against economic loss/damage due to future, contingent events/perils simply belies any attempt to place annuities within the ambit of the term 'insurance.' Insurance companies may well be allowed to sell annuities, just as they are sometimes allowed to make loans, but they are not engaging in the 'business of insurance' when they do so."

App. 35a-36a.

Judge Flaum then turned from the literature to the caselaw. Noting that *NationsBank* was the most relevant authority on the issue, he also invoked

other cases in this Court.[5] Judge Flaum then turned to the nature of the risk involved in "insurance." He pointed out that in more recent cases, this Court has

> "continued to emphasize that the risk transferred by 'insurance' must be an *insurance* type risk, not just any old risk: 'Both the "spreading" and the "underwriting" of risk refer in this context to the transfer of risk *characteristic of insurance.*"

App. 42a (emphasis Judge Flaum's), quoting *Pireno*, 458 U.S. at 130; and further citing this Court's language in *Group Life & Health Ins. Co.* v. *Royal Drug Co.*, 440 U.S. 205, 211 n.7 (1979), that "insurance must protect against 'loss or damage by a contingent event' or by a 'specified contingency or peril.'" *Ibid.*

The necessity for a "contingent event or peril" led Judge Flaum to discuss the inadequacy of the *Pireno* factors for determining the type of question here presented, and the need for this Court's further guidance. App. 43a-48a. He pointed out that

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[5] These included *Helvering* v. *Le Gierse*, 312 U.S. 531 (1941), with its discussion of the contrast between the "insurance risk" of true insurance and the "investment risk" of annuities, App. 39a-40a, and *VALIC*, *supra*, as to which he noted that the "issue at stake" was not "mortality risk" but "the necessity of financial risk-taking on the part of the insurance company." App. 40a-42a. He noted that the majority's "attempts to find in *VALIC* a formula for 'insurance' *i.e.* insurance = mortality risk + guaranteed return," ran counter to this Court's "expressed intent" in *VALIC* not to provide a comprehensive definition of "insurance." App. 42a n.17. He also noted that the majority's characterization of a "risk of declining returns in times of depression" as a "risk in the insurance sense" was specifically rejected by this Court in *VALIC*. *Ibid.*, quoting 359 U.S. at 71.

the decisions of this Court have not been about the problem in this case, which is "the regulation of federal entities under state insurance codes"; instead, they have dealt with "attempted regulation of state-licensed insurance companies under federal securities and antitrust laws." App. 43a. This difference in focus, he pointed out, shows the limitations of the *Pireno* test. "The most relevant part of the test," he noted, "is the first criterion—whether the practice has the effect of transferring or spreading a policyholder's risk—but it alone cannot be decisive." App. 47a. In summing up, he reemphasized that this Court "has always been considering insurance company practices," and "has not yet considered a case ... where a state properly regulated the conduct of a non-insurance company under its McCarran-Ferguson power to regulate 'the business of insurance.'" App. 48a.

Finally, Judge Flaum turned to the question "whether McCarran-Ferguson trumps the countervailing federal principle," just reaffirmed in *Barnett Bank*, "that the banking activities of national banks are governed by federal law and generally should not be interfered with by the states"—what he called the "long and lofty" "tradition against allowing state intrusion into the activities of national banks," no matter how well-intentioned and motivated by consumer protection such state intrusion might be. App. 49a. He pointed to *Barnett Bank*'s emphasis "that the history of national bank jurisprudence has been one of reading national bank powers broadly and minimizing state interference with the exercise of these powers." App. 53a, citing 116 S. Ct. at 1108-109. He rejected the majority's view that *Barnett Bank* had "ma[de] some kind of broad statement that McCarran-Fergu-

son normally trumps the National Bank Act," App. 54a, for *Barnett Bank*, he said, involves "a *convergence*, rather than a conflict, between the National Bank Act and McCarran-Ferguson ... ." *Ibid.* (emphasis original). Moreover, he pointed out that, contrary to the majority's statement here, the National Bank Act involves no "intrusion" into state regulation. "*This case is about state intrusion into federal banking business, not about federal intrusion into state control of the insurance business.*" App. 54a n.29 (emphasis added). "*Barnett Bank*'s primary relevance for our inquiry is its strong affirmation of the presumed power of national banks to engage in banking activities free from state interference." *Ibid.*

To drive the point home, Judge Flaum reviewed in detail the OCC's determination that the Retirement CD is an exercise of a national bank's express powers, concluding that this determination fully comported with the standards set forth in *NationsBank* and *Chevron*. App. 56a-62a. In conclusion, he said:

> "After considering the full import of the Supreme Court's unanimous decision in *NationsBank*, 115 S. Ct. 810 (1995), I simply cannot accept the majority's conclusion that the selling of an annuity by a national bank constitutes 'the business of insurance' under McCarran-Ferguson. While the *NationsBank* opinion did not address the precise question before us, its analysis, its tone, and the sources relied upon all compel the inference that annuities are not truly 'insurance,' and thus that a national bank selling them is not engaged in 'the business of insurance.' The modern literature on insurance powerfully affirms this conclusion, and the history of insurance caselaw is in accord. In addition, the long and established tradition

> against allowing state intrusion into the affairs of national banks cautions against too readily condoning the present regulation by the State of Illinois."

App. 62a-63a.

III. REASONS FOR ALLOWANCE OF THE WRIT

The decision below is inconsistent with this Court's decisions in *NationsBank* and *Barnett Bank*, and with the decision of the Eighth Circuit in *First Nat'l Bank of Eastern Arkansas* v. *Taylor*, 907 F.2d 775 (8th Cir.), *cert. denied*, 498 U.S. 972 (1990). It points up the need for this Court to make it clear that states cannot, under the guise of "insurance regulation," interfere with conduct of a national bank that the federal regulator has explicitly recognized to be within the bank's express core powers. In a time of change in both the banking and insurance industries the issues involved here are of compelling public importance.

A. The Majority Opinion Is Inconsistent With This Court's Decision in *Barnett Bank* and With a Decision of the Eighth Circuit.

As noted *supra*, *Barnett Bank* dealt with whether a state could forbid a national bank from exercising the power granted by 12 U.S.C. § 92 to sell insurance in small towns. In a unanimous opinion by Justice Breyer, this Court held that state law could not forbid such activity.

Justice Breyer's opinion first discussed in some detail the historic immunity of national banks from state interference with the exercise of their powers, describing that history as "one of interpreting grants of both enumerated and incidental 'powers' as grants of authority not normally limited by, but

rather ordinarily pre-empting, contrary State law." 116 S. Ct. at 1108. The cases, he said, "take the view that normally Congress would not want States to forbid, or to impair significantly, the exercise of a power that Congress specifically granted." *Id.* at 1109. "[W]here Congress has not expressly conditioned the grant of 'power' upon a grant of state permission, the Court has ordinarily found that no such condition applies." *Ibid.*[6]

The opinion then turned to the asserted "reverse preemption" of McCarran-Ferguson. Though holding that § 92 "specifically relates to the business of insurance," Justice Breyer did not rest the Court's decision on that ground alone. Rather, he rested it on McCarran-Ferguson's "language *and purpose, taken together*," 116 S. Ct. at 1111 (emphasis added). That purpose, he said, was *not*—

> "to insulate state insurance regulation from the reach of all federal law. Rather, [McCarran-Ferguson] seeks to protect state regulation primarily against *inadvertent* federal intrusion—say, through enactment of a federal statute that describes an activity in broad, general terms, of which the insurance business happens to comprise one part."

Id. at 1112 (emphasis original). "The circumstances surrounding enactment of the McCarran-Ferguson Act suggest the same," he continued. *Ibid.*[7] His

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[6] The opinion cited and discussed such classic cases to this effect as *Franklin Nat'l Bank* v. *New York*, 347 U.S. 373 (1954); *First Nat'l Bank of San Jose* v. *California*, 262 U.S. 366 (1923); and *Easton* v. *Iowa*, 188 U.S. 220 (1903).

[7] Those circumstances were that *South-Eastern Underwriters* had disclosed for the first time that the adoption of the Sherman Act in 1890 had inadvertently intruded into the insurance arena; "inadvertently," because in 1890 insurance

description of the primary motivation of McCarran-Ferguson as having been to correct and avoid "inadvertent" and unexpected intrusions into the state-regulated insurance field by broad general federal statutes contrasts sharply with his extensive discussion of the affirmative purposes of national bank legislation a few pages earlier.

Unlike the Sherman Act, the National Bank Act is not a broad regulation of commerce that was later found to have inadvertently impinged upon state regulation. *It is not, in fact, a federal "regulation" of anything.* It creates federally chartered banking corporations, subjects them to federal supervision to the exclusion of state "visitation," 12 U.S.C. § 484, and authorizes them to go about their business. There was nothing "inadvertent" or "unanticipated" about the National Bank Act. Congress knew exactly what it was doing: It was helping to finance the Civil War and put the nation's finances on a sound basis, see generally HAMMOND, BANKS AND POLITICS IN AMERICA 718-732 (1957), by affirmatively creating federal corporations for federal purposes—corporations the exercise of whose express powers "Congress would not want States to forbid, or to impair significantly ... ." 116 S. Ct. at 1109.

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was widely believed not to be interstate commerce, and to be subject to state but not federal regulation. "In reaction to *South-Eastern Underwriters*, Congress moved quickly, enacting McCarran-Ferguson to restore the supremacy of the States in the realm of insurance regulation." *Id.* at 1112 (citations and internal quotation marks omitted). "But," he continued, "the circumstances we have just described mean that '*restoration*' [emphasis original] of 'supremacy' basically required setting aside the *unanticipated* effects of *South-Eastern Underwriters*, and cautiously avoiding similar *unanticipated interference* with state regulation in the future." *Ibid.* (emphasis added).

Adding to this the fact that in 1864, when the National Bank Act was adopted, Illinois was not regulating annuities under its insurance laws and would not do so for another half-century,[8] we submit that the majority's reliance on *Barnett Bank* here is diametrically opposite to its correct interpretation—as Judge Flaum's dissent made clear.

There is, we submit, a potentially even broader issue here; one that fits squarely within the commonsense analysis of *Barnett Bank*. Some federal statutes deal with matters of such "paramount importance," *Moore* v. *Nat'l Distillers and Chemical Corp.*, 143 F.R.D. 526, 534 (S.D.N.Y. 1992) (magistrate judge's decision), to the national interest that Congress cannot conceivably have intended to turn them over to the states however broad the language of McCarran-Ferguson may be. See *Moore*, *supra* (though Foreign Sovereign Immunities Act nowhere relates to business of insurance, McCarran-Ferguson preemption inapplicable in view of paramount importance of U.S. foreign policy concerns embodied in the FSIA). Would the Congress that enacted McCarran-Ferguson in the spring of 1945 have thought it was allowing a state to authorize a domestic company to insure German and Japanese ships notwithstanding the Trading with the Enemy Act? Obviously not. The Legal Tender Act nowhere mentions insurance; could a state require that insurance premiums be paid only in gold and silver? Obviously not.

On essentially this basis, the Eighth Circuit held that McCarran-Ferguson preemption does not apply

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[8] According to Brief for Respondent in *NationsBank*, at p. B1, Illinois' definition of annuities as "insurance" dates from 1911 ILL. LAWS 377, § 1.

to the National Bank Act. *First Nat'l Bank of Eastern Arkansas* v. *Taylor*, *supra*. There, a national bank in Arkansas offered "debt cancellation contracts" under which, for an additional payment, a debt would be cancelled if the borrower died before it was repaid. The OCC had ruled that such contracts were a lawful exercise of the powers of a national bank. The Insurance Commissioner of Arkansas, however, took the position that they were the equivalent of credit life insurance policies and were subject to his jurisdiction under McCarran-Ferguson. The Eighth Circuit held squarely that McCarran-Ferguson preemption was inapplicable:

> "We hold that because the debt cancellation contracts offered by FNB fall within the incidental powers[9] granted by the National Bank Act, they do not constitute the 'business of insurance' under the McCarran-Ferguson Act."

907 F.2d at 779. Foreshadowing *Barnett Bank*, the Eighth Circuit reached this conclusion in part because the longstanding exclusive federal regulation of national banks prior to McCarran-Ferguson "strongly indicates that Congress did not intend the 'business of insurance' to encompass lawful activities of national banks." *Id.* at 780.

In light of *Barnett Bank*, we submit that the Eighth Circuit in *Taylor* was plainly right, and the Seventh Circuit in the present case was plainly wrong. This Court should make that clear.

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[9] *A fortiori* where, as here, *express* and not merely *incidental* national bank powers are involved.

B. The Majority Opinion's Holding That Annuities Are Insurance Is Inconsistent With This Court's Decision in *NationsBank*.

The majority opinion is clearly inconsistent with *NationsBank*. There, this Court dealt with the question whether national banks can sell annuities as agents or brokers for the actual issuers. The OCC had ruled that they can do so, as an activity "incidental" to "the business of banking" under the National Bank Act, 12 U.S.C. § 24 Seventh. The suggestion had been made that national banks could only do so in towns of under 5,000 people, on the reasoning (a) that annuities are insurance, and (b) 12 U.S.C. § 92, by expressly authorizing national banks in such towns to sell insurance, implies that national banks in larger towns may not do so. The OCC rejected this contention, taking the view that annuities are not "insurance." The majority of the Fifth Circuit panel disagreed, holding that annuities are insurance on *precisely* the same reasoning as that of the majority in this case—including that annuities "are the mirror image of life insurance," 998 F.2d at 1301, *compare* the majority here, App. 11a; that they transfer and spread "mortality risk," *ibid.*, *compare* the majority here, App. 11a-12a; and that the states "regulate annuities under their insurance laws," *id.* at 1300, *compare* the majority here, App. 14a.[10]

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[10] "Essentially," said the majority here, "lifetime annuities such as the Retirement CD are the 'mirror image' of life insurance policies." App. 11a. "[T]he person who purchases a lifetime annuity," it said, "insures against no longer having sufficient money produced by his assets." App. 13a. An annuity, it said, "insures the purchaser against a decline in the market ... . The purchaser is given the comfort that should a depression occur in the market, causing rates of interest to fall

Rejecting this reasoning, and upholding the OCC's determination for a unanimous Court under the *Chevron* doctrine, Justice Ginsburg said:

> "[A]nnuities are widely recognized as ... investment products. See D. SHAPIRO & T. STREIFF, ANNUITIES 7 (1992) (in contrast to life insurance, 'annuities ... are primarily investment products'); 1 J. APPLEMAN & J. APPLEMAN, INSURANCE LAW AND PRACTICE § 84, p. 295 (1981) ('Annuity contracts must ... be recognized as investments rather than as insurance.')."

115 S. Ct. at 814-15. She continued:

> "By making an initial payment in exchange for a future income stream, the [annuity] customer is deferring consumption, setting aside money for retirement, future expenses, or a rainy day. For her, an annuity is like putting money in a bank account, a debt instrument, or a mutual fund. Offering bank accounts and acting as agent in the sale of debt instruments and mutual funds are familiar parts of the business of banking. ... ."
>
> "In sum, modern annuities, though more sophisticated than the standard savings bank

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significantly, he will not suffer a 'loss' of future income, but will continue to receive the rate of interest guaranteed in his Retirement CD contract." *Ibid.* On this reasoning, of course, *every fixed-rate security* is "insurance." Moreover, as we show at p. 22 *infra*, *NationsBank* explicitly rejected the notion that the presence of "mortality risk" necessarily qualifies an investment as insurance. The majority did not mention this fact or make any effort to deal with it. Nor did the majority make any effort to discuss the cases—literally scores of them—which have consistently held, for well over a century, in every conceivable context, that absent some special statutory definition annuities are not insurance. See note 11 *infra*.

> deposits of old, answer essentially the same need. By providing customers with the opportunity to invest in one or more annuity options, banks are essentially offering financial investment instruments of the kind congressional authorization permits them to broker."

115 S. Ct. at 815-16 (citations omitted).

The opinion rejected the argument that annuities must be insurance because they "traditionally have been sold by insurance companies":

> "But the sale of a product by an insurance company does not inevitably render the product insurance. For example, insurance companies have long offered loans on the security of life insurance, see 3 APPLEMAN & APPLEMAN, INSURANCE LAW AND PRACTICE §1731, at 562 (1967), but a loan does not thereby become insurance."

Ibid. Justice Ginsburg also rejected the argument that annuities must be insurance because "most States have regulated annuities as insurance." "[A] characterization fitting in certain contexts may be unsuitable in others," she said, and state classification of annuities as insurance is generally done in the context of "defining the powers of insurance companies and state insurance regulators." In other settings, "States have resisted lump classification of annuities as insurance." *Id.* at 816.

Most significantly, the Court's opinion examined and rejected the very argument relied on by the majority here, that annuities must be insurance because they involve a "mortality risk." This Court said:

> "[T]he presence of mortality risk does not necessarily qualify an investment as 'insurance' under § 92. For example, [the respondent] recognizes that a life interest in real property is not insurance, although it imposes a mortality

> risk on the purchaser. Tr. of Oral Arg. 42. Some conventional debt instruments similarly impose mortality risk. See Note, *Reverse Annuity Mortgages and the Due-on-Sale Clause*, 32 STAN. L. REV. 143, 145-151 (1979)."

Ibid. Further distinguishing annuities from insurance, this Court said:

> "A key feature of insurance is that it indemnifies loss. See BLACK'S LAW DICTIONARY 802 (6th ed. 1990) (first definition of insurance is 'contract whereby, for a stipulated consideration, one party undertakes to compensate the other for loss on a specified subject by specified perils'). As the Comptroller observes, annuities serve an important investment purpose and are functionally similar to other investments that banks typically sell. ... And though fixed annuities more closely resemble insurance than do variable annuities, fixed annuities too have significant investment features and are functionally similar to debt instruments."

Ibid. (citations omitted). In sum, said Justice Ginsburg:

> "We ... defer to the Comptroller's reasonable determination that 12 U.S.C. § 92 is not implicated because *annuities are not insurance* within the meaning of that section."

Id. at 817 (emphasis added).

This holding was absolutely consistent with the overwhelming number of decided cases holding that (absent a special statutory definition) annuities are not insurance.[11] It was also absolutely consistent

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[11] Judge Flaum's discussion of the legal literature, in which these dozens of cases are cited and discussed, powerfully amplifies this point. J. APPLEMAN & J. APPLEMAN, INSURANCE LAW & PRACTICE 84, p. 295 (1981), he noted, was twice relied

with the settled definition of insurance as involving *indemnity* against a risk of *loss*—"loss or damage by

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on in *NationsBank*; he reviewed at length, App. 28a-29a, its discussion of why, in its words (quoted in *NationsBank*, 115 S. Ct. at 815), "Annuity contracts must, therefore, be recognized as *investments rather than as insurance.*" App. 29a (emphasis Judge Flaum's). He pointed out that COUCH, CYCLOPEDIA OF INSURANCE LAW (2d ed. 1983), was relied on by this Court in *Pireno* and *Royal Drug*, and that it has a whole section entitled "Annuity as Distinguished From Insurance." App. 29a-30a. Moving on to the legal encyclopedias, he quoted at considerable length from CORPUS JURIS SECUNDUM, App. 30a-33a, commenting that it "does an excellent job of illuminating the distinction between annuities and true insurance products," including such telling phrases as "[a]n annuity is not an indemnity against loss of death, but is essentially a form of investment, " App. 30a, and "[a]n annuity is a provision for life with *no indemnity feature* ..., and it is *not based on contingency of loss.*" App. 31a (emphasis Judge Flaum's). He then reviewed AM. JUR. to the same effect. App. 33a. Turning to BLACK'S LAW DICTIONARY and WEBSTER'S NEW INTERNATIONAL DICTIONARY, both of which he noted had been cited by this Court in *NationsBank* and *Royal Drug*, he quoted their definitions at some length. App. 33a-35a. The sole treatise Judge Flaum found that "appear[ed] to place at least some annuities within the realm of 'insurance,' " App. 36a, was KEETON & WIDISS, INSURANCE LAW (1988). He considered, however, that KEETON's definition "raises substantial questions," App. 37a, noting that KEETON did not explain what the other commentators found decisive:

> "why a product that provides for payment 'upon the occurrence of' some specified event (*i.e.*, beginning with that event), as insurance does, should be treated as equivalent to a product that provides for payment 'as long as' or until some specified event occurs (*i.e.*, ending with that event), as an annuity does."

App. 37a. KEETON, he added, says that refund annuities are even more like investments than are traditional annuities; he said that perhaps Keeton himself would not call the Retirement CD insurance. App. 38a. We note that KEETON cites no authority for its analysis—unlike APPLEMAN, COUCH, AM. JUR., and C.J.S., all of which cite a plethora of cases. As Judge Flaum points out, KEETON conflicts with the rest of the literature and with the caselaw (including *NationsBank* in this Court).

a contingent event... ." *Royal Drug*, 440 U.S. at 211-12 n.7. And the caselaw is abundantly clear that annuities do not involve such a *risk* or any *indemnity*, and that this is precisely why they are not insurance.[12] *Moreover, the courts and commentators agreed in 1945 as they do today that annuities were not insurance, and it was against this backdrop that McCarran-Ferguson was enacted.*

The majority's dismissal of the controlling significance of *NationsBank* is, we submit, indefensible. It ignored everything that underlay Justice Ginsburg's analysis: that insurance entails indemnity against risk while annuities do not; that "mortality risk" does not make an arrangement insurance; and, finally, the overwhelming caselaw and commentary to the effect that annuities are not insurance. And it ignored the fact that the majority's reasoning was exactly that of the Fifth Circuit panel that was reversed in *NationsBank*.

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[12] *E.g.*, *Corporation Commission* v. *Equitable Life*, 73 Ariz. 171, 239 P.2d 360, 363, 365 (1951) ("annuity contracts...are not a 'risk' based on contingency of loss. ... Risk refers to a hazard which is not an element of an annuity contract, and involves a chance of loss not present in such a contract, as it is in a policy of insurance"); *In re Barr's Estate*, 104 Cal. App. 2d 506, 231 P.2d 876, 878 (Calif. App. 1951) ("an annuity is not insurance. Both insurance and annuity are, it is true, gambles against the contingency of death. They are dissimilar, however, in that under an annuity the company's obligation is not to indemnify on the happening of a contingent event causing loss," quoting 1 R. PAUL, FEDERAL ESTATE AND GIFT TAXATION 498); *Gregg* v. *Commissioner*, 315 Mass. 704, 54 N.E.2d 169, 172-73 (1944); *Daniel* v. *Life Ins. Co. of Virginia*, 102 S.W.2d 256, 260 (Tex. Civ. App. 1937).

C. The Majority Opinion's Attempt To Apply the "*Pireno* Test" Emphasizes the Need for This Court To Clarify Criteria For Identifying "Insurance" Under McCarran-Ferguson.

NationsBank's discussions of indemnity against loss and the nature of an insurance risk tie in closely with the "*Pireno* test." [13] We repeat its three criteria:

> "*[F]irst*, whether a practice has the effect of transferring or spreading a policyholder's risk; *second*, whether the practice is an integral part of the policy relationship between the insurer and the insured; and *third*, whether the practice is limited to entities within the insurance industry."

458 U.S. at 129.

In the courts below, the parties wrestled with the application of the *Pireno* test to the case at bar. It is the only test available and the lower courts naturally try to apply it. But, as Judge Flaum's dissent makes clear, Procrustean efforts are necessary to try to make it fit a case like the present one, where the question is not whether ancillary activities of a state-chartered insurance company are part of "the business of insurance," but whether a particular type of federally-approved contract offered by a federally-chartered non-insurance entity is a

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[13] That test stems from *Royal Drug*, which involved the question whether a health insurer's drug procurement contracts were part of the "business of insurance," and was restated in *Pireno*, which involved the same question for an insurer's "peer review" procedure for evaluating claims under a policy.

contract of "insurance."[14] More important, it was not formulated for, and has never been applied to, the question whether activity that the federal regulatory authority has determined fall within the express core powers of a federally chartered national bank constitutes "the business of insurance."

Three comments about *Pireno* in this context are appropriate.

First (as is immediately evident from the way the second criterion is formulated), the test presupposes an insurance policy and an insured. In other words, it is structured for the question whether ancillary conduct of an insurance company (not a federally chartered corporation) is part of McCarran-Ferguson's "business of insurance." As Judge Flaum noted, App. 48a, that is the only situation in which this Court has ever applied it. It was not formulated for, and has never been applied by this Court to, the question whether a contract by a non-insurance entity is a contract of insurance.

Second, *Pireno* is explicit that the first criterion refers not to "just any old risk," as Judge Flaum phrased it, App. 42a, but to a special kind of risk, an *insurance* risk. "Both the 'spreading' and the 'underwriting' of risk refer in this context to the transfer of *risk characteristic of insurance.*" 458 U.S at 130 (emphasis added). We note yet once more that that "characteristic" risk is the risk of "loss or damage by a contingent event ... ," *Royal*

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[14] We believe, needless to say, that the Retirement CD is not the "business of insurance" under any reasonable application of the *Pireno* test. It does not transfer an *insurance* risk, and many, many non-insurance entities, ranging from medieval potentates to the United States government to Vassar College, have issued them and issue them today.

Drug, 440 U.S. at 211-12 n.7, and that this is simply not a feature of annuities.

Lastly, the scope of the third criterion is unclear. As applied in *Pireno* itself and in *Royal Drug* before that, it reflected the fact that non-insurance entities (chiropractors and pharmacists, respectively) participated in the specific allegedly anticompetitive arrangements before the Court. Both the majority and the dissent in the case at bar, however, read this criterion as directed either at whether a practice is *inherently* one that could be engaged in only by an insurance industry entity, or at whether it is one that is *in fact* engaged in (*de facto* or by statutory monopoly) exclusively by such entities.[15] Judge Flaum did, however, recognize that it was unsuited for determining whether the federally approved conduct of national banks fell within McCarran-Ferguson. This uncertainty once again

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[15] Either way, annuities do not fit this criterion. The United States issues literally hundreds of thousands of annuities in the form of pensions and otherwise. *E.g.*, 28 U.S.C. § 376 (annuities for survivors of judicial officials). They are issued as funding mechanisms by thousands of such obviously non-insurance entities as United Way of America, Vassar College, and the Southern Baptist Convention, see *Charities That Offer Gift Annuities Catch Flak for Uniform Rates*, WALL ST. JOURNAL, October 5, 1995, p. A1, and Congress has explicitly recognized this fact by taxing annuities issued by insurance companies differently from those issued by others. 26 U.S.C. § 1275(a)(1)(B)(i) and (ii). "Ever since the American Bible Society entered into the first planned giving arrangement in the 1830s, charitable gift annuities have been a traditional method of giving in America." 141 CONG. REC. S9306 (June 28, 1995) (Senator Hutchison). The insurance industry's own trade press says that "insurance departments in [only] 11 states ... regulate charitable gift annuities as insurance." *Texas Gift Annuities Suit Not Likely To Dim Sales*, NATIONAL UNDERWRITER, Oct. 16, 1995, 4 at 45.

reflects the fact that the *Pireno* test was designed only for evaluating practices ancillary to contracts that are concededly insurance policies issued by insurance companies.

We believe, of course, that annuities, including the Retirement CD, are, as the OCC has effectively determined, clearly not insurance under any reasonable test. The important point here, however, is that *Pireno* needs to be clarified by clear guidance from this Court in the context of situations where the issue is whether an activity by a federally chartered non-insurance entity is "the business of insurance" for McCarran-Ferguson purposes.

D. The Issues Involved Are of Broad Public Importance.

A tectonic shift is taking place in the life insurance industry. The traditional keystone of life insurance companies' business was "whole life" insurance. While life insurance companies have long issued annuities, this was traditionally a sideline activity, like that of lending money.[16] But whole life insurance has lost its appeal in an age of inflation and enhanced life expectancy; insurance agents are leaving the business in great numbers; and life insurance companies have turned to a new emphasis on annuities. See, *e.g.*, *Retired, Finally, But Still Saving for Tomorrow*, NEW YORK TIMES, October 1, 1995, p. 1; *Could This Be You? That's the Pitch, As Insurers Revive Focus on Death*, NEW YORK TIMES, September 28, 1995, p. D1. Mean-

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[16] Only 15 years ago, the leading treatise could say: "The volume of insurance written annuities is presently negligible ... ." 1 APPLEMAN & APPLEMAN, INSURANCE LAW AND PRACTICE § 81, at 285-86 (1981).

while, banks are showing new "creativity and innovation," as Judge Wood's concurring opinion noted, App. 19a; and life insurance companies and agents have (not surprisingly) mounted a sustained drive to prevent national bank competition both generally and with particular reference to annuities. In each of the last two Terms, in *NationsBank* and again in *Barnett Bank*, this drive has reached this Court, and in both cases the efforts to limit national banks' authority has been unanimously rejected. The present case affords an opportunity to settle questions of great importance in this area, and to forestall the massive attack on national banks' exercise of their federally conferred powers, in the guise of "insurance regulation," that is certain to result from the Seventh Circuit's decision.

IV. CONCLUSION

Judge Flaum's thorough and scholarly dissent is in a real sense a call for this Court's help from a distinguished court of appeals judge. He points out the need to address the relationship between McCarran-Ferguson and the National Bank Act; the majority's failure to follow this Court's decisions in *NationsBank* and *Barnett Bank*; and the the need for an appropriate test rather than the *Pireno* test for cases like the one at bar. We respectfully urge that his call be heeded, and that the petition for certiorari be granted.

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